



**DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
STATE OF HAWAII**

Audit of Expenditures
For the Quarter Ended September 30, 2003

Internal Audit Report No. 05-08

AUDIT DIVISION
Department of
Accounting and General Services
July 11, 2005

EXECUTIVE SUMMARY

The Department of Accounting and General Services, Audit Division conducted an audit of the Department of Accounting and General Services' (the Department) expenditures for the quarter ended September 30, 2003 to determine whether expenditure payments made by the Department are legal, recorded to the proper account, in compliance with applicable laws, rules and regulations, policies and procedures, and established accounting procedures and internal controls.

The mission of the Department is to maintain the State's accounting records, administer capital improvement projects, maintain the State's information and communications systems, and provide professional and technical expertise to state agencies.

The Department includes other activities such as school repairs and maintenance, establishing procurement policies, statewide internal auditing, public building maintenance, office leasing, performing and visual arts, the Aloha Stadium, election services, campaign spending monitoring, survey services, archive services, parking and motor pool services, risk management, and others.

With respect to the audit of the Department's expenditures, we noted the following:

- A professional services award was not in compliance with Section 103D-304(i), Hawaii Revised Statutes (HRS), which requires the award to be posted electronically within seven days of the award date by the chief procurement officer.
- A modular workstation purchased at a cost of \$5,912.80 was not reported to the State Procurement Office as required by Section 103D-1206, HRS.
- Three competitive sealed bid contracts awarded in 2001, 2002, and 2003 for the procurement of services did not have written evidence of compliance with the posting of awards requirement pursuant to Section 3-122-33(e), HAR.
- The process to procure goods, services, and construction under Act 316, State Laws of Hawaii (SLH) 2001, is performed by the Physical Plant Operations and Maintenance Services Branch (AGS 807) engineers and other employees who are not procurement specialist. AGS 807 employees developed the required written policies and procedures for the State Comptroller. The written policies and procedures do not provide the necessary guidelines and instructions to properly procure goods, services, and construction. Without sufficiently detailed written procedures, problems are inevitable.
- We found three instances in which the contractor was issued two or more purchase orders for the same school, same type of service, but different amounts less than \$100,000.00. In each instance, purchase orders combined exceeded the \$100,000.00 exemption allowed by Act 316, SLH 2001. The projects were parceled to avoid competitive bidding or competitive proposals.

We recommend that the Department establish controls to comply with the Sections 103D-304(i), 103D-1206, HRS, and Act 316, SLH 2001, and report the parceling procurement violation to the State Procurement Office.

In response, the Department concurs with the audit findings and will establish controls to comply with Sections 103D-304(i), 103D-1206, HRS, and Act 316, SLH 2001, and report the parceling procurement violation to the State Procurement Office..

**DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES
STATE OF HAWAII**

TABLE OF CONTENTS

	<u>Page</u>
I. INTRODUCTORY SECTION	
Letter of Transmittal	1
Summary	2
Introduction	2
Background	2
Scope, Objectives, and Methodology	2
Audit Procedures Performed	3
II. NONCOMPLIANCE SECTION	
Audit Findings with Recommendations:	
Audit Finding No. 1 – Professional Services Award – Posting of Award	5
Audit Finding No. 2 – Proper Recording of Capital Assets	6
Audit Finding No. 3 – Competitive Sealed Bid – Posting of Award	6
Audit Finding No. 4 – Policies and Procedures	7
Audit Finding No. 5 – Parceling of Project Costs	8
III. DEPARTMENT’S RESPONSE	

I. INTRODUCTORY SECTION

LINDA LINGLE
GOVERNOR



Russ K. Saito
Comptroller

Katherine H. Thomason
Deputy Comptroller

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING
AND GENERAL SERVICES

P.O. BOX 119
HONOLULU, HAWAII 96810-0119

AUD 05.0125

July 11, 2005

Mr. Kerry Yoneshige
Administrative Services Officer
Department of Accounting and General Services
State of Hawaii
1151 Punchbowl Street, Room 414
Honolulu, Hawaii 96813

Dear Mr. Yoneshige:

In accordance with the provisions of Section 26-6 of the Hawaii Revised Statutes, I present you with a financial audit report on the Department of Accounting and General Services' expenditures for the quarter ended September 30, 2003.

The report is presented in two sections: introductory and noncompliance. The introductory section includes this transmittal letter, a summary of services, introduction, background, scope, objectives, methodology, and audit procedures performed. The noncompliance section includes a schedule of audit findings with recommendations.

Sincerely,

A handwritten signature in black ink, reading "Russ K. Saito".

RUSS K. SAITO
State Comptroller

SUMMARY

The Department of Accounting and General Services (the Department), Audit Division conducted an audit of the Department's expenditures for the quarter ended September 30, 2003 to determine whether expenditure payments made by the Department are legal, recorded to the proper account, in compliance with applicable laws, rules and regulations, policies and procedures, and established accounting procedures and internal controls.

INTRODUCTION

Authority to conduct this audit resides in Section 26-6, Hawaii Revised Statutes (HRS), which authorizes after-the-fact audits to determine the legality of expenditures and the accuracy of the accounts. In addition, Section 40-2, HRS, requires the State Comptroller to ensure that all accounting procedures and internal controls of departments in the executive branch of the State government adhere to prescribed policies and procedures and accounting principles generally accepted in the United States of America.

This audit is part of the Audit Division's 2004-2005 Audit Plan. The Audit Division is not independent with respect to the Department of Accounting and General Services.

Audit fieldwork took place October 8, 2004 through December 3, 2004 at the Department's fiscal office at 1151 Punchbowl Street, Honolulu, Hawaii. Rod B. Catiggay, CPA, Supervising Auditor, conducted the audit under the supervision of Wayne L. Chu, CPA, Audit Division Administrator.

BACKGROUND

The Department was created in 1959 by the Hawaii State Government Reorganization Act of 1959 (Act 1, Second Special Session Laws of Hawaii 1959). The primary functions of the Department is to maintain the State's accounting records, administer capital improvement projects, maintain the State's information and communications systems, and provide professional and technical expertise to state agencies.

The Department includes other activities such as school repairs and maintenance, establishing procurement policies, statewide internal auditing, public building maintenance, office leasing, performing and visual arts, the Aloha Stadium, election services, campaign spending monitoring, survey services, archive services, parking and motor pool services, risk management, and others.

SCOPE, OBJECTIVES, AND METHODOLOGY

The audit includes an examination of expenditures paid by the Department during the period July 1, 2003 through September 30, 2003. The audit objectives are to determine the legality of expenditures, accuracy of accounts, and the Department's compliance with established accounting procedures and internal controls.

Department of Accounting and General Services
Audit of Expenditures Report – Quarter Ended September 30, 2003

This report includes detail testing of a sample of expenditure transactions and does not include the Department's other financial transactions, such as payroll expenditures, cash receipts and journal vouchers (JVs). The audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

A listing of the Department's expenditures for the quarter ended September 30, 2003, from the State's Financial Accounting and Management Information System, was used for sampling and verification to source documents during the audit. The Department processed for payment 13,176 expenditure transactions totaling \$699,875,977.98 during the quarter ended September 30, 2003.

We examined 50 randomly selected expenditure transactions, totaling \$354,105.20, as outlined below:

	<u>Total Population</u>	<u>Sample Items</u>	
		<u>Count</u>	<u>Amount</u>
Expenditures	\$23,071,711.01	43	\$258,058.74
Contract expenditures:			
Competitive bid	55,758,662.06	6	83,961.64
Professional services	6,009,335.34	1	12,084.82
Payroll expenditures and JVs	<u>615,036,269.57</u>	<u>-</u>	<u>-</u>
Totals	<u>\$699,875,977.98</u>	<u>50</u>	<u>\$354,105.20</u>

To gain an understanding of the Department's procedures in processing expenditures for payment and documenting the internal controls related to those procedures, we interviewed appropriate personnel, reviewed applicable available written policies and procedures, and documented our understanding of the established accounting procedures and internal controls in place during the audit period.

AUDIT PROCEDURES PERFORMED

We reviewed documents supporting expenditures such as vendor's invoices, purchase orders, summary warrant vouchers, requisition forms, procurement documents, contracts and inventory records to determine compliance with applicable laws, rules and regulations, policies and procedures, and compliance with established accounting procedures and internal controls.

Based on our detail testing of expenditure transactions, we found 43 expenditures and 7 contract expenditures to be legal expenditures of the Department, properly recorded and processed by the Department, and in compliance with established accounting procedures and internal controls, except for the 5 audit findings presented in the noncompliance section of the report.

II. NONCOMPLIANCE SECTION

AUDIT FINDINGS WITH RECOMMENDATIONS

The procedures enumerated below were performed to determine whether payments made by the Department are legal, recorded to the proper account, in compliance with applicable laws, rules and regulations, policies and procedures, and established accounting procedures and internal controls.

AUDIT FINDING NO. 1 – PROFESSIONAL SERVICES – POSTING OF AWARD

Section 103D-304(i), HRS, states that contracts awarded under this section for \$5,000 or more shall be posted electronically within seven days of the contract award by the chief procurement officer or designee and shall remain posted for at least one year. The State Procurement Office (SPO) established a database of professional services awards on its website to assist departments and State agencies to satisfy this statutory requirement and electronically post their contract awards.

We noted one professional services contract awarded by the Audit Division that did not have acceptable written evidence of compliance with Section 103D-204(i), HRS, in the project file. The contract was awarded in May 2002. No acceptable written evidence was in the project file attesting that the award was electronically posted within 7 days of the date of the award.

In 2001 and 2002, SPO's website did not display the posting date of the professional services awards. In January 2005, SPO modified its presentation of professional services awards to include the posting date. However, the awards made in 2001 and 2002 are no longer on the current SPO's listing of professional services awards.

Procedures Performed

We interviewed the administrator and employee that participated in the procurement of the project. We examined the contract project files. We reviewed SPO's website of professional services awards.

We found an unsigned written notation that the contract award was posted electronically to the SPO's website within 7 days of the date of the award. However, this evidence was not sufficient to show compliance with Section 103D-304(i), HRS.

Recommendation

The Department shall establish a control to comply with Section 103D-304(i), HRS. A copy of the document showing complete compliance with this section shall be placed in the project file.

AUDIT FINDING NO. 2 – PROPER RECORDING OF CAPITAL ASSETS

Section 103D-1206, HRS, requires departments and State agencies to report annually the costs of capital assets purchased during the fiscal year to the SPO.

The State Foundation on Culture and the Arts (SFCA) purchased a modular workstation at a cost of \$5,912.80 during the audit period. This expenditure meets the State's policy of recording the workstation as a capital asset of the State. SFCA did not report the workstation as a capital asset to the State Procurement Office as required Section 103D-1206, HRS.

Procedures Performed

We interviewed the employee responsible to report annually the costs of capital assets purchased during the fiscal year to the SPO. We examined SFCA's annual report (Annual Summary of Inventories Report – AGS Form 17B) to the SPO for the fiscal year 2004.

The workstation was not included in the annual report to the SPO for the fiscal year 2004.

Recommendation

SFCA shall establish a control to report the cost of the workstation to the State Procurement Office as required by Section 103D-1206, HRS. Failure to comply with this section will result in penalties as stated in Section 103D-1209 and Section 103D-1210, HRS.

Section 103D-1209, HRS, states that if any officer, head of department, agent, employee, or other person fails to file the required inventory within the time prescribed, the SPO's administrator shall withhold the salary or wage due the officer, head of department, agent, employee, or other person until the inventory is filed.

Section 103D-1210, HRS, imposes a \$500 penalty or imprisonment of not more than six months for any officer, member of a public board, assessor, or other person who fails to perform any of the duties imposed upon the person by these sections.

AUDIT FINDING NO. 3 – COMPETITIVE SEALED BID – POSTING OF AWARD

Section 3-122-33(e) of the Hawaii Administrative Rules (HAR), states that the award shall be issued to the lowest responsive bidder whose bid meets the requirements and criteria set forth in the invitation for bids and posted pursuant to Section 103D-701, HRS, for 5 working days.

We noted three contracts awarded in 2001, 2002, and 2003 through the competitive sealed bid process for the procurement of services that did not document compliance with the posting of awards requirement pursuant to Section 3-122-33(e), HAR.

Procedures Performed

We interviewed the Department's staff that participated in the procurement of the three contracts obtained through the competitive sealed bid process and examined the contract project files for written evidence of compliance.

We did not find written evidence in the contract project files that the awards were posted for 5 working days.

Recommendation

The Department shall establish a control to comply with Section 3-122-33(e), HAR. A copy of the document showing complete compliance with this Section shall be placed in the project file.

AUDIT FINDING NO. 4 – POLICIES AND PROCEDURES

Act 316, Section 2(e), State Laws of Hawaii (SLH) 2001, states that the expenditure of funds for any project with an estimated total cost of less than \$100,000 shall be exempt from Chapter 103D and Section 464-4 provided that the comptroller shall develop internal policies and procedures for the procurement of goods, services, and construction.

The process to procure goods, services, and construction under Act 316, SLH 2001, is performed by the Physical Plant Operations and Maintenance Services Branch (AGS 807) engineers and other employees who are not procurement specialist. AGS 807 employees developed the written policies and procedures for the State Comptroller. The policies and procedures consist of three pages.

Procedures Performed

We obtained a copy of the written policies and procedures. Through inquiry and observation, we documented the major procedures used to procure goods, services, and construction by AGS 807.

We noted that the written policies and procedures do not provide the necessary guidelines and instructions to properly procure goods, services, and construction. The actual procedures used are not in written form.

Recommendation

AGS 807 should document its policies and procedures to procure goods, services, and construction under Act 316, SLH 2001, in a more detailed manner. The employees who procure goods, services, and construction are not procurement specialists and procurement is a small portion of their responsibilities. They need clear, concise, and easy to follow procedures to enable them to perform their jobs and comply with the Act 316, SLH 2001.

AUDIT FINDING NO. 5 – PARCELING OF PROJECT COSTS

Act 316, Section 2(e), SLH 2001, states that the expenditure of funds for any project with an estimated total costs of less than \$100,000.00 shall be exempt from Chapter 103D and Section 464-4 provided that the procurement requirements shall not be artificially divided or parceled so as to avoid competitive bidding or competitive proposals.

Procedures Performed

We interviewed AGS 807 personnel who have knowledge or perform the procedures to procure goods, services, and construction for the repair and maintenance of school facilities. We reviewed written policies and procedures and rules and regulations as well as applicable State laws. We performed analysis of POs awarded to contractors. We reviewed documents such as purchase orders and payments.

We found three instances in which the contractor was issued two or more separate purchase orders (PO) for the same school, same type of service, but with different PO amounts less than \$100,000.00. In each instance, the purchase orders together exceed the \$100,000.00 exemption allowed by Act 316, SLH 2001. The projects were parceled to avoid competitive bidding or competitive proposals.

Recommendation

AGS 807 shall develop written policies and procedures to comply with Act 316, SLH 2001, to prevent future occurrences that prevent competition, create multiple expenditures at the inception of the project to evade the requirements of Act 316, SLH 2001, and to artificially divide or parcel the procurement requirements so as to constitute a small purchase.

In addition, AGS 807 should report its parceling violations and noncompliance with Act 316, SLH 2001, to the State Procurement Office (SPO) by completing SPO Form 16, *Procurement Violation: Report of Findings and Corrective Actions*, as required by Section 3-131-6, Hawaii Administrative Rules.

III. DEPARTMENT'S RESPONSE

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

Response to Audit Findings
Quarter ended September 30, 2003

Audit Finding No. 1 – Professional Services Award – Posting of Award

A professional services award was not in compliance with Section 103D-304(i), Hawaii Revised Statutes (HRS), which requires the award to be posted electronically within seven days of the award date by the chief procurement officer.

Recommendation

We recommend that the Department establish controls to comply with the Section 103D-304(i).

Department's Response

The Department concurs with the audit finding and recommendation.

Department's Corrective Action Plan

The Department plans to implement the following procedures and controls:

1. The Department will adopt a policy, which requires that screen prints documenting the date of input of the award be approved by the administrator of the division, office, and attached agency to document compliance.
2. Education of the Department's divisions, offices, and attached agencies.
 - a. A memorandum will be prepared to advise and remind the administrators and managers of the new policy and the requirements of Section 103D-304(i), HRS. The memorandum will include procedures to comply with this HRS section.

Audit Finding No. 2 – Proper Recording of Capital Assets

A modular workstation purchased at a cost of \$5,912.80 was not reported to the State Procurement Office as required by Section 103D-1206, HRS.

Recommendation

We recommend that the Department establish controls to comply with the Section 103D-1206, HRS.

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

Response to Audit Findings, Continued

Department's Response

The Department concurs with the audit finding and recommendation.

Department's Corrective Action Plan

The Department plans to implement the following procedures and controls:

1. Education of the Department's divisions, offices, and attached agencies.
 - a. A memorandum will be prepared reminding the administrators and managers of the requirements of Section 103D-1206, HRS. The memorandum will include procedures to comply with this HRS section.
2. Communications.
 - a. A listing will be provided semi-annually to each division, office, and attached agency of capital asset expenditures that have not been recorded in the inventory system. The division, office, attached agency will note the disposition of the unrecorded items and remit the listing to the Administrative Services Office (ASO).
 - b. A memorandum will be attached to the listing to remind the administrators and managers of the requirements of Section 103D-1206, HRS.
3. Follow-up.
 - a. Semi-annually, the list of expenditures made for capital expenditures not recorded in the inventory system received from the divisions, offices, and attached agencies will be reviewed by the ASO to ensure a disposition of the unrecorded item.
 - b. This semi-annual report will be placed in the files.

Audit Finding No. 3 – Competitive Sealed Bid – Posting of Award

Three competitive sealed bid awards were not in compliance with Section 103D-701, HRS and Section 3-122-33(e), HAR which requires the award to be posted for five working days.

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

Response to Audit Findings, Continued

Recommendation

We recommend that the Department establish controls to comply with Section 103D-701, HRS and Section 3-122-33(e), HAR. A copy of the document showing complete compliance with these sections shall be placed in the project file.

Department's Response

The Department concurs with the audit finding and recommendation.

Department's Corrective Action Plan

The Department plans to implement the following procedures and controls:

1. The Department will adopt a policy, which requires that a copy of the award letter be posted on the bulletin board between the Personnel Office and the State Procurement Office for five working days. The administrator of the division, office, and attached agency will need to verify the posting by signing a copy of the award letter to document compliance and filed in the contract folder.
2. Education of the Department's divisions, offices, and attached agencies.
 - a. A memorandum will be prepared to advise and remind the administrators and managers of the new policy and the requirements of Section 103D-701, HRS and Section 3-122-33(e). The memorandum will include procedures to comply with these sections.

Audit Finding No. 4 – Policies and Procedures

Act 316, Section 2(e), SLH 2001 allows Central Services Division (CSD), Physical Plant Operations and Maintenance Services Branch, AGS-807 an exemption from Chapter 103D and Section 464-4 for any project with an estimated total cost of less than \$100,000 provided that the Comptroller develop internal procurement policies and procedures. The written policies and procedures developed by the CSD do not provide the necessary guidelines and instructions to properly procure goods, services, and construction. The actual procedures used are not in written form.

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

Response to Audit Findings, Continued

Recommendation

We recommend that the AGS 807 program document its policies and procedures to procure goods, services, and construction under 316, SLH 2001 in a more detailed manner. Since the purchases are done by non-procurement specialists, clear, concise, and easy to follow procedures are needed.

Department's Response

The Department concurs with the audit finding and recommendation.

Department's Corrective Action Plan

The Department plans to implement the following procedures and controls:

1. Although the AGS-807 program for Oahu is transferring to the Department of Education (DOE) on July 1, 2005, and no longer exempt from Chapter 103D under Act 316, SLH 2001, the Department will have the CSD review and amend their existing policies and procedures related to Chapter 103D, HRS, if necessary and have the State Procurement Office review and comment on their procurement procedures.
2. Education and Training of the CSD Employees
 - a. All of the CSD personnel involved in the procurement process will be required to visit SPO's website @http://www.hawaii.gov/spo/SPO/code/index_html immediately to obtain and review the training materials.
 - b. After the revised procurement policies and procedures are completed, all appropriate staff will receive training from the State Procurement Office.
3. The DOE will be apprised of this audit finding for their appropriate action.

Audit Finding No. 5 – Parceling of Project Costs

Three instances were discovered in which the contractor was issued two or more separate purchase orders (PO) for the same school, same type of service, but with different PO amounts less than \$100,000. In each instance, the POs together exceeded the \$100,000 exemption allowed by Act 316, SLH 2001.

STATE OF HAWAII
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

Response to Audit Findings, Continued

Recommendation

We recommend that the AGS 807 program develop written policies and procedures to comply with Act 316, SLH 2001 and not artificially divide or parcel the procurement requirements so as to constitute a small purchase. Additionally, the program should report its noncompliance to the State Procurement Office by completing the SPO Form 16, Procurement Violation: Report of Findings and Corrective Actions, as required by Section 3-131-6, HAR.

Department's Response

The Department concurs with the audit finding and recommendation.

Department's Corrective Action Plan

The Department will immediately file the SPO Form 16 to the State Procurement Office to report the procurement violations and plans to implement the following procedures and controls to prevent future reoccurrences:

1. Although the AGS-807 program for Oahu is transferring to the DOE on July 1, 2005, and no longer exempt from Chapter 103D under Act 316, SLH 2001, the Department will have the CSD review and amend their existing policies and procedures related to Chapter 103D, HRS, if necessary and have the State Procurement Office review and comment on their procurement procedures.
2. Education and Training of the CSD Employees
 - a. All of the CSD personnel involved in the procurement process will be required to visit SPO's website @http://www.hawaii.gov/spo/SPO/code/index_html immediately to obtain and review the training materials.
 - b. After the revised procurement policies and procedures are completed, all appropriate staff will receive training from the State Procurement Office.
3. The DOE will be apprised of this audit finding for their appropriate action.